

A REPORT OF THE CSIS
PROJECT ON U.S. LEADERSHIP
IN DEVELOPMENT

Maximizing Development of Local Content across Industry Sectors in Emerging Markets

HOW PRIVATE-SECTOR SELF-INTEREST CAN HELP
U.S. DEVELOPMENT POLICY

Authors

Michael Levett
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1

INTRODUCTION

While the promise is still far greater than the reality, strategies and programs built on the positive impact on development from private-sector initiatives in frontier and emerging markets is gaining acceptance and driving change in corporate boardrooms and NGO projects. Multinational corporations (MNCs) engaged in these initiatives represent sectors as diverse as extraction and agriculture, tourism and technology, and pharmaceuticals and electronics. Corporations point to their balance sheets as the motivation for policies, projects, and practices that create businesses, jobs, national and family wealth, and new economic opportunities across the developing world. While these outcomes have long been the goal of international donors and development organizations, it now appears that the private sector may be better prepared to accomplish many of them using their own funds, skills, and practices—and with motivations that are less lofty.

The power of the private sector to have a positive impact on development has frequently been unrecognized or undervalued by many members of the traditional development community, and viewed as an unintended or irrelevant consequence by MNCs. As Holly Wise and Sokol Shtylla explained it, “As Milton Friedman might say, ‘the business of business is business’—and this is exactly what gives firms the capability and credibility to expand economic opportunity. Business activity creates jobs, cultivates inter-firm linkages, enables technology transfer, builds human capital and physical infrastructure, generates tax revenues for governments and, of course, offers a variety of products and services to consumers and other businesses. Each of these contributions has multiplier effects on development.”¹

Recognition of the relatively few corporate business strategies and programs that include the positive impact on development—or the potential for private-sector-driven development—could not come at a more propitious time. As MNCs and other businesses continue to expand the global reach of their supply chains and resource acquisitions and increasingly require new markets for sale of their products, materials, and services, the budgets of the United States Agency for International Development (USAID) and other international aid agencies are, at best, holding steady and are, more probably, decreasing. These parallel realities hold the promise of expanded economic opportunities, benefits and stability for men and women in many countries of tremendous economic need and social stress using far fewer, better targeted and integrated resources of development agencies and donor groups.

MNCs impact development in many ways: from their large investments to their corporate social responsibility programs, from direct hiring to technology and skills. However, nowhere are the current and potential activities of large companies more dynamic and influential on development than through their local-content policies, programs, and practices. Nothing matches the scope and

1. Holly Wise and Sokol Shtylla, “The Role of the Extractive Sector in Expanding Economic Opportunity,” Harvard Kennedy School of Government, 2007, http://www.hks.harvard.edu/m-rcbg/CSRI/publications/report_18_EO%20Extractives%20Final.pdf, p. 4.

impact of the continuing demand by large global companies for both supply-chain inputs and new markets for their products and services along with the financing available to meet the demand.

Business counts among its bottom-line arguments for local-content strategies the potential to reduce the costs and time needed to obtain goods and services as well as the creation of a supportive operating environment. The latter argument—“reducing risk” or “obtaining a social license to operate”—has been more important to companies in the extractive industry or manufacturing than building positive name identification or helping to meet host-government operating mandates. However, the value of positive name identification becomes even more important as U.S. and European companies find that their plans for expanding sales depend on countries labeled “developing,” or “emerging market,” or “frontier.” Over time, the most powerful argument may be a play on the oft-told Henry Ford tale of his willingness to pay workers the outrageous sum of \$5 per day not for their own good, but so that they would be able to buy Ford automobiles. Local-content strategies may be seen as Ford writ large: if MNCs are to sell to local markets, the residents of those countries must be part of successful economies and afford to buy the MNCs’ goods and services.

Local small and medium-size enterprises (SMEs) that currently lack access to the global supply chain, and small farmers who do not meet the requirements of large agricultural buyers, have the chance to benefit from corporate investments in training, infrastructure build-out, and changes in corporate procurement policies. These initiatives make it easier for small farmers to have their products aggregated with those of their neighbors and purchased by large buyers, as well as for small businesses to compete for and win supply-chain contracts. There is nowhere that U.S. government agencies can have greater impact and influence on immediate and near-term development activities than through targeted, need-driven, timely interventions that fill gaps in corporate potential, such as training, facilities, access to information and financing, or technology. The costs of filling these gaps can be far less than traditional economic development programs; however, given the scale, scope, and duration of corporate involvement as a buyer or end-user, the total expenditures benefiting local businessmen and women can dwarf those of the traditional development programs.

Will large private-sector companies benefit from U.S. government participation? Absolutely. Is this troubling to some in the development community? Certainly. But most importantly, local companies, employees, and families will benefit at a higher level and on a continuing basis, as can—depending on the initiative or project—local and national governments through expanded tax revenues, improved physical infrastructure, expanded access to technologies and know-how, and more capable, competitive companies that meet domestic commercial and consumer demand.

Corporate purchasing or sourcing of local goods, services, and raw materials, and the programs and practices that expand opportunities for more SMEs to enter the global supply chain, are not the only high-impact activities overtaking donor dollars for scale and scope. Indeed, direct foreign investment and remittances both surpass traditional sources of development funding. But local content and local-content development are the “low-hanging fruit” of private-sector development. The very corporate rules and processes that create barriers to entry into the supply-chain world also provide the opportunity for the SMEs that can overcome those barriers.

Businesses must buy goods and services, products, and labor required for their supply chains from one source or another and they create policies, develop practices, and take significant time to support their procurement “spend.” The argument for “business value” in putting that spend

into local content now can justify a pro-development strategy for what is already inevitable use of corporate resources.

The potential for local content can be found in almost every sector, but any recognition of its strategic role as a development tool is “stove-piped” on a sector-by-sector basis. This “stove-piping” leads to undervaluing the entire arena, and results in a failure to share lessons learned across sectors, take advantage of assets and resources created by local-content development in one sector, or make changes in policies and practices that would support “donor intervention” development financing.

Local-content development may operate in one sector under the flag of government mandates, while activities in another sector may be identified with corporate social responsibility or with the more ambiguous social license to operate. And any of these drivers may continue to motivate expansion of local content. *The expansion of local-content-for-development activities—growth in number of supporting companies, breadth of sectors being considered, approaches, or the overall type of content—is becoming noticeably more prominent in private and public spheres. But as that is happening, corporations are increasingly pointing to corporate strategic planning and bottom-line business practice as the prime movers for investing in the expansion of local content.*

The time is now to support existing and endorse new private-sector strategies, programs, and practices that expand economic development in emerging and frontier markets, while informing and shaping U.S. government policies and practices that stimulate and assist selected private-sector activities. To do so, we must understand what motivates the private sector today, what creates barriers to such activities, and what will drive future expansion.

This report makes broad policy recommendations that apply to the general use of a local-content strategy by the private-sector companies and the U.S. government agencies such as USAID that historically provide technical assistance and the Millennium Challenge Corporation (MCC) and the Overseas Private Investment Corporation that can take positions that maximize local economic opportunities and growth. Key recommendations include the following:

- Nothing makes the point better than successful practice. The U.S. government’s own procurement and contracting regulations and practices should seek to realize the full benefits of local sourcing. (USAID should be recognized for recently changing some policies to expand local sourcing. At the same time, MCC has maintained a “source-neutral” procurement policy; it would appear worthwhile for MCC to study how its procurement practices could strengthen local capacity in the sectors where it invests.)
- U.S. government agencies should identify and use opportunities that build on and support private-sector initiatives that enhance the creation of local businesses, jobs, and economic opportunities—maximizing the development impact of MNCs’ local-content initiatives with targeted, timely interventions that are specific to the sector, country, and project. Such a use of donor dollars and donor know-how is the basis of a “do more with less” strategy.
- U.S. government agencies should seek to maximize their role as (1) a convener of all stakeholders in high-potential development activities in order to build on corporate plans and the variety of available resources; (2) a creator of development policy that includes roles for the private sector; and (3) a motivator and funder for projects that build local-content-friendly legislative and regulatory environments for both local SMEs and MNCs in host countries.

Our goal was to examine why and how the private sector, nongovernmental development actors, and the U.S. government, particularly USAID, can employ policies and practices to expand local content in order to drive economic development and create economic opportunities. Accordingly, this report identifies and highlights the development benefits of a local-content strategy while recognizing the commercial benefits of such a strategy accruing to large participating companies. In chapter 2, the report uses three case studies to identify existing successes and challenges. Chapter 3 provides recommendations for those businesses and government agencies as well as host governments working on local-content development, and chapter 4 provides the conclusion.

2

CASE STUDIES

The following are three case studies from three very different business sectors—extraction (oil and gas), tourism, and agriculture. Naturally, there are many inherent differences in the basic components of each sector—most obvious, perhaps, the products and services that multinational or major local companies need and will be purchasing along their specific supply chains that will ultimately combine to meet the demands of their customers. *But it is the shared elements of the case studies that begin to create the picture of potential for private-sector-driven development:*

- The international private sector's need to purchase identified goods or services;
- The international private sector's recognition of the value to their businesses of using local suppliers;
- The international private sector's ability to spend time and money to ensure the (quality) participation of local entrepreneurs and farmers as suppliers;
- Inputs from NGOs;
- Local companies and farmers getting and taking advantage of the opportunity to provide those goods and services;
- Continuing participation in and contribution to local economies by the private sector because of the ongoing demands and purchasing power of the “buyers”; and
- Continuing benefits (revenues) going to SMEs as well as governments at multiple levels.

The three case studies demonstrate: the drivers and motivations of the various players; the strategies and (consistently well-timed) planning; the alliances and various roles of the different participants; the implementing practices and key benefits and results; and many of the lessons learned in bringing the concepts to reality. Perhaps most important, the case studies demonstrate that (1) the corporate business driver-targeted intervention approach is not limited to one sector, to one type of local business or entrepreneur, or to one size end-user or corporate beneficiary; (2) the small businesses, farmers, and local economies continue to benefit without the need for new or continuing public or donor funds; and (3) the approach will contribute to the sustainable development outcomes called for in the administration's development policy.

Case Study 1—Extraction Sector: Oil and Gas and SME Development in Angola

Background

Oil was discovered in Angola in 1910 with the first well drilled in 1915.² By 2010, Angola surpassed Nigeria as sub-Saharan Africa's largest oil-producing country (17th in the world).³ The country is now China's second-leading source for crude oil and one of the top suppliers to the United States.⁴

The oil industry is not labor intensive from the standpoint of operations. Even though resource extraction does not produce many direct jobs—the oil sector runs heavily on contracts—it does generate economic returns⁵ that can be appropriated by national governments. The high standards and quality requirements of the oil industry make it difficult for local companies to meet the procurement needs of international oil companies (IOCs) and their first-tier, largely international suppliers. Because IOCs frequently import manpower and materials, local companies are often unable to reap the benefits of the oil sector.⁶ Most oil-producing nations, including Angola, have responded to this practice by enacting national mandates requiring the IOCs to source or hire locally as a part of their license to operate. However, both the policies and their implementation vary dramatically between countries.

Drivers

When Angola's 27-year civil war ended in 2002, the country was left with a significant human capital deficit and a nonfunctioning economy apart from oil and gas, which constituted 76 percent of the country's GDP in 2000.⁷ The Angolan government responded by introducing a local content initiative that required oil companies to hire Angolans and source from locally run businesses.⁸ The war, however, created an environment where the oil industry could not do business under the conditions set by the initiative because of the dearth of qualified local enterprises. Business development services (BDS) were also significantly underdeveloped, which compounded this shortage of suppliers.⁹ With the “Angolanization” mandate for IOCs to source locally, an entity was needed to assist local businesses in growing their technical capacity.

2. Angolan Embassy in Canada, “History of Oil in Angola,” last modified May 25, 2011, <http://www.embangola-can.org/oil.html>.

3. Central Intelligence Agency, *World Factbook*, “Country Comparison—Oil Production,” last modified December 7, 2011, <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2173rank.html>.

4. U.S. Department of State, “Background Note: Angola,” Bureau of African Affairs, October 13, 2011, <http://www.state.gov/r/pa/ei/bgn/6619.htm>.

5. The payment to a factor of production in excess of what is required to keep that factor in its present use. David R. Henderson, “Rent Seeking,” *The Concise Encyclopedia of Economics*, Library of Economics and Liberty, <http://www.econlib.org/library/Enc/RentSeeking.html>.

6. CDC Development Solutions, “Angola: A Legacy for Supply Chain and Local Content Development,” CDS Supplier Training Initiative, <http://www.cddevelopmentalsolutions.org/cds-supplier-training-initiative>.

7. EarthTrends, “Economic Indicators—Angola,” EarthTrends Country Profiles, 2003, http://earthtrends.wri.org/pdf_library/country_profiles/eco_cou_024.pdf.

8. U.S. Department of State, “Background Note: Angola.”

9. U.S. Agency for International Development/South Africa, *Developing the Supply of Financial Services and Improving the Efficiency of the Banking Sector in Angola*, submitted by the Services Group, Inc., and Nathan Associates, January 2008, http://pdf.usaid.gov/pdf_docs/PNADX263.pdf.

Activities

CDC Development Solutions (CDS), an international NGO that specializes in linking global supply chains and local enterprise development, began working with the Angolan oil industry's stakeholders in 2003 to "improve the capacity and competitiveness of local companies in Angola that could serve as contractors and suppliers to the oil industry."¹⁰ The first step was to conduct a gap analysis of the country's SMEs.¹¹ Juxtaposing the commercial needs of IOCs with the capabilities of the Angolan business community, the research revealed six major components necessary to foster local businesses capable of working with the oil industry:

- Training programs specifically geared toward the requirements of the IOCs were needed;
- Local businesses would benefit from the provision of on-site business assistance—including technology and knowledge transfers;
- Information about the IOCs' procurement needs and the availability of SMEs to meet that demand and a system to communicate it were necessary in order to link the budding supply of oil with the industry's demand;¹²
- An enterprise development center (EDC) should be developed;
- Expanded access to finance was needed to allow the businesses to expand; and
- The success of local businesses required the active participation of and partnership between the IOCs, EDC, and the participating SMEs, with the Angolan government's overarching approval.¹³

Initially working with BP and the Angolan Ministry of Petroleum, CDS developed a comprehensive strategy to increase the ability of local companies to compete as suppliers to the oil industry.¹⁴ In 2005, representatives from the Angolan state-run company, Sonangol P&P, and IOCs represented by BP, Chevron, ExxonMobil, and Total,¹⁵ established the *Centro de Apoio Empresarial* (CAE) to serve as the recommended EDC. The oil companies provided the capital and the market demand,¹⁶ while CDS was contracted to run CAE.

10. CDC Development Solutions, "Angola: A Legacy for Supply Chain."

11. According to the Private Enterprise Partnership for Africa (PEP Africa), supply chain development should involve four steps: consultation/supply chain assessment, gap analysis of specific sector, gap-specific design of technical assistance needs, and then implementation of supply-chain development programs. Michael Hackenbruch, "Local Content and Supplier Development—A conceptual toolkit," International Finance Corporation and PEP Africa, October 2006, http://www.menas.co.uk/App_Data/elib/Michael%20Hackenbruch.pdf.

12. CDS also proposed that a "unit" would be necessary to "house a database listing local companies possessing the capacity to serve the oil and gas industry and facilitate linkages between SME businesses." CDC Development Solutions, "Angola: A Legacy for Supply Chain."

13. CDC Development Solutions, "Angola: A Legacy for Supply Chain and Local Content Development," *News from CDC Development Solutions: Development Solutions*, April 2010, <http://www.cdcdevelopmentsolutions.org/sites/default/files/DSApril2010.pdf>.

14. CDC Development Solutions, "Supply Chain Development: CAE—Apoio Empresarial Transfers to Local Control," January 2011, <http://www.cdcdevelopmentsolutions.org/January2011CAEandSupplyChain>.

15. These five companies made up the enterprise development subcommittee of the Angolan Government's Local Content Initiative.

16. Business Action for Africa and Harvard Kennedy School: Corporate Social Responsibility Initiative, *Business Partnerships for Development in Africa: Redrawing the boundaries of possibility*, 2010, http://www.hks.harvard.edu/m-rcbg/CSRI/publications/BAAREport_2010.pdf.

One of the goals of CAE was to produce a functioning, and eventually sustainable, market of local enterprises to meet the mandated needs of IOCs.¹⁷ Once up and running, CAE improved the capacity of Angolan SMEs to serve as contractors and suppliers and then prepared them to bid for oil-industry contracts.¹⁸ Initially, CAE's services ranged from assisting SMEs with financial analysis and business training to the specific elements associated with the provision of goods and services needed by the oil industry.¹⁹

To receive CAE services, SMEs serving the oil industry must either have 100 percent Angolan ownership or be a joint venture with at least 50 percent Angolan participation.²⁰ Successful SMEs are then indexed on CAE's Certified Supplier Directory that details the strengths of individual enterprises, including their current capacity in areas relating to the oil industry. CAE clients tend to be a part of the "missing middle," meaning they are too big to qualify for microfinance but too risky for mainstream financial services. In 2010, CAE expanded its client services and created the program "Access to Finance (A2F)" to help *qualified* SMEs gain access to capital, often vital to implement contracts they have captured and their largest constraint to growth.²¹ Also in 2010, Chevron funded an Angolan business plan competition for local entrepreneurs. CAE contributed by running a five-week intensive course for fourteen CAE-certified companies to prepare business plans.²²

Results

CAE strengthened Angola's supply chain network and improved the ability of Angolan enterprises to source to the IOCs. By the project's end, more than 1,500 Angolan-owned businesses had participated in the CAE program through training and technical assistance, 124 companies were certified as suppliers for the oil industry, and some 300 contracts and contract extensions resulted from CAE involvement.²³ CAE generated more than \$214 million in oil-industry contracts, while supporting the creation of more than 2,700 Angolan jobs.²⁴

17. CDC Development Solutions, "Angola: A Legacy for Supply Chain"; and Business Action for Africa, *Business Partnerships for Development in Africa*.

18. Business Action for Africa, *Business Partnerships for Development in Africa*; CDC Development Solutions, "Angola: A Legacy for Supply Chain"; USAID, *Developing the Supply of Financial Services*.

19. USAID, *Developing the Supply of Financial Services*.

20. These businesses also had to be operational for one year or more before applying and be a legally registered and legitimate company (e.g., no shell companies). CDC Development Solutions, "News from CDC Development Solutions"; and CAE Apoio Empresarial/Angola, "Developing Local Content in the Angolan Oil & Gas Industry," http://www.caeangola.com/home_en.html.

21. CDC Development Solutions, "Supply Chain Development: CAE—Apoio Empresarial Transfers to Local Control."

22. Chevron Human Energy, *Cabinda Gulf Oil Company Limited: 2010 Corporate Responsibility Report*, <http://www.chevron.com/documents/pdf/2010-AngolaCR-English.pdf>.

23. USAID, *Developing the Supply of Financial Services*.

24. U.S. Center for Citizen Diplomacy, "5 Questions for Member Organization," CDC Development Solutions," <http://uscenterforcitizendiplomacy.org/blog/entry/5-questions-for-member-organization-cdc-development-solutions-20110829/>.

The A2F program succeeded in increasing awareness and knowledge of financial services and helped SMEs create innovative investment and lending models.²⁵ This CAE project led to the publishing and distribution of the first guide to financing instruments available for SMEs in Angola, *Financiamento em Angola*.²⁶

The business plan competition culminated with a \$7,500 award to the top two plans.²⁷ The three CAE-certified Angolan companies benefited not only from having comprehensive business plans, but also from the connections they made with local banks and potential buyers.²⁸ This competition was touted as a success by Chevron.²⁹

Some of the SMEs trained by CAE have gone on to become larger-scale operations thriving as a result of the oil industry's needs. For example, NASA Commercial Import and Export Ltd. has provided personal protective equipment (PPE) for the oil industry in Angola for the past 10 years,³⁰ growing from a two-person outfit to a staff of 20.³¹ Prompted by Chevron, NASA was one of the first clients at CAE, which provided training including financial management, human resource management, bidding, and contracting. NASA was CAE certified in 2008 and is now Cabinda Gulf Oil Company Ltd.'s (CABGOC) supplier of safety shoes and coveralls under contracts totaling more than \$5 million.³² NASA's additional contracts include ones with Halliburton, Schlumberger, Vector Gray, Inc., Petromar, and Alllead Energy.³³

Another successful CAE trainee is Luafanda Reparações, LDA, an Angolan plumbing and electrical SME. Prior to receiving CAE services, Luafanda Reparações was run by an independent contractor and performed small jobs for clients in and around Luanda.³⁴ The business was referred to CAE for help with essential tasks like crafting invoices, as well as advance financing to purchase the necessary supplies. Luafanda received technical assistance and training for more than a year and transformed into a company capable of taking advantage of the growing services market in Luanda. In 2010, the company won a \$680,000 contract with BP for the repair and maintenance of stairway lights in a modern high-rise in Luanda.³⁵

25. CDC Development Solutions, "Access to Finance for Development."

26. "Finance in Angola" is a financing guide for SMEs. See Chevron Human Energy, *Cabinda Gulf Oil Company Limited: 2010 Corporate Responsibility Report*.

27. CDC Development Solutions, "News from CDC Development Solutions."

28. The three winners of the first business plan event were Casa Temaf, a family-owned hotel chain; Angolan Purchasing & Supply, a Soyo-based service provider; and Pembele Comércio, a supplier of personal protective equipment. Angolan Purchasing & Supply was able to make two valuable bank contacts that have agreed to finance the business up to \$300,000. CDC Development Solutions, "Access to Finance for Development."

29. Ibid.

30. Chevron Human Energy, *Cabinda Gulf Oil Company Limited: 2010 Corporate Responsibility Report*.

31. CAE Apoio Empresarial, "Small Family Business Becomes Multi-Million Dollar Supplier," *Strengthening Relationships with the Oil & Gas Industry*, http://caeangolanews.weebly.com/uploads/3/6/6/4/3664955/historia_de_sucesso_-_nasa_-_eng.pdf, accessed March 21, 2012.

32. Chevron Human Energy, *Cabinda Gulf Oil Company Limited: 2009 Corporate Responsibility Report: Enabling Economic Development in Angola*, 11, <http://www.chevron.com/documents/pdf/AngolaCReenglish.pdf>, and CDC Development Solutions, "Access to Finance for Development."

33. CDC Development Solutions, "Access to Finance for Development."

34. Luanda is where Angola's sole refinery, which is operated by Sonangol, is located. U.S. Department of State, "Background Note: Angola," October 13, 2011, <http://www.state.gov/r/pa/ei/bgn/6619.htm>.

35. CAE Apoio Empresarial, "Small Family Business Becomes Multi-Million Dollar Supplier."

Committing its efforts to ensuring the sustainability of the project, CDS focused from the beginning on employing, training, mentoring, and empowering the CAE staff with the aim of eventually transitioning the project, including its leadership, to the Angolans.³⁶ On January 1, 2011,³⁷ in conjunction with Sonangol and the Ministry of Petroleum, and in association with the Angolan Chamber of Commerce and Industry, CAE was officially under the direction of an Angolan director.³⁸ Rather than “simply being an enabler,” the nationalization of CAE is itself evidence of the growth of local content in Angola.³⁹

Lessons Learned

Local Content Strategy—CAE

Beginning with the end in mind, this program leveraged the assets of each participating actor: the Angolan government, IOCs, and CDS. CAE had the Angolan government’s approval, and the funding that IOCs provided to CDS for CAE helped to fill the capacity gap, something the IOCs were less than unanimously inclined to do on their own. In the five years that CAE used third-party technical assistance, it grew into a functioning and Angolan-run entity that built a portion of the country’s SME capacity up to international standards.

Increasing SMEs’ access to credit also helped to address the disconnect between the local banking sector and Angolan SMEs. The funds generated for SMEs allowed them to expand, enabling them to better compete with larger foreign firms working with the extractive industry.⁴⁰ Growing the number of qualified local SMEs helped to put downward pressure on the rising prices associated with the increased demand.⁴¹

CAE acted as a space for the providers of goods and services to share information and ideas for streamlining the supply chain.⁴² “CAE is a ‘great example’ of the power of an EDC to grow the local supply chain and illustrates the impact of this kind of mutually beneficial partnership,” stated CDS.⁴³

Many of the lessons CDS applied in Angola were learned in earlier local content development projects that were funded totally, or in part, by USAID both in the Russian Far East and in Azerbaijan. In the latter setting, the U.S. government accepted CDS assurances that a two-year investment by USAID would not only produce new contracts, jobs, and skills, but would also result in one or more of the IOCs creating their own follow-on programs. Following the successful two-year program, BP created its own enterprise center that continued to upgrade the capacities and the contract captures of local firms.

36. Business Action for Africa, *Business Partnerships for Development in Africa*.

37. CDC Development Solutions, “Supply Chain Development: CAE—Apoio Empresarial.”

38. *Ibid.*

39. This information is from a quote by John Lindley, BP’s vice president of procurement and supply chain management. Lindley, who helped create CAE, is a significant proponent the program. CDC Development Solutions, “Angola: A Legacy for Supply Chain.”

40. CAE, “Supply Chain Development,” program presentation.

41. *Ibid.*

42. *Ibid.*

43. CDC Development Solutions, “Angola: A Legacy for Supply Chain.”

Starting small is more than acceptable but aiming high is an imperative. The first win of a local content program may be around very basic services—food, security, transportation, or cleaning—but the goal should be to move as quickly as possible to greater upstream, midstream, and downstream opportunities. At various stages, all “streams” can include fabrication and construction, logistics, operations support, and professional services, consulting, business office support. The key to meaningful, sustainable success is the move from the basic and manpower services to fabrication, construction, and such while recognizing that not all activities are equal in their impact on local content. Construction impacts job creation more than subservice activities, while subservice activities have a greater impact on innovation and technology transfers than do logistics or maintenance.

Involving all stakeholders—IOCs, first-tier suppliers, national and local government agencies, local SMEs and trade associations, business services providers—from the earliest stages possible allows for greater understanding of both existing procurement patterns and real-world barriers to expanding local content and will deliver outcomes with far greater efficiency and effectiveness. Establishing targets and benchmarks; monitoring, evaluating performance, and adjusting on-the-ground; and integrating best practices are vital to success.

Transparent, open, fair, and accountable procurement policies and practices of the IOCs—with a free flow of information and equal opportunities for local firms to compete and win—can have a positive effect on public perception of the role of those oil majors in the nation’s economy and society. And they create the opportunity for a more pervasive effect on the public’s expectation of how business and government can operate in the best interests of the citizenry.

While there are frequent assumptions that expanding local content for the oil sector will reduce costs and increase timeliness of delivery of goods, this is not always the case. Over time, as local firms become practiced contractors and develop the skills and expertise they are introduced to in training and consulting sessions, costs should fall and speed should increase. Experience shows that these are not always the most compelling arguments for early-stage local content development projects, but rather mandates, risk insurance, and social license to operate are more often employed.

Working with local and national governments is as important as it can be complicated. While a lack of quality, basic, early education may be a problem in many resource-heavy nations being targeted by extraction companies, there is too often a lack of coordination between government agencies that if overcome could produce significant benefits to local firms and individuals who want to compete for supply chain contracts. For example, if the IOCs sit down with both the Ministry of Petroleum and the Ministry of Education, the result could be business education and skills training programs—at universities and vocational-technical schools—that would significantly minimize the need for later development projects (e.g., Intel in Costa Rica and Penang).

Local Content Strategy—Chevron

CAE was one of several lines of activity that involved the IOCs, Angolan government, third-party NGOs such as CDS, and the United States through USAID. In addition to CAE, Chevron funded programs that provided technical assistance to more than 3,000 farmers through the creation of

around three dozen associations (Angola Partnership Initiative)⁴⁴ and helped create NovoBanco, a thriving micro- and small-business finance institution.⁴⁵

CAE and the other initiatives listed above illustrate the benefits—for both local economies and the IOCs—of a procurement strategy that invests in and then utilizes local resources. As a result of its experience in Angola, Chevron took steps to shift its strategy—in some areas of operation—from a more transactional approach to a longer-term one based on early engagement, alliances, and inclusivity with its supply chain.⁴⁶ The long-term benefits of these programs justified Chevron’s investment of time and money, and the company now publicly claims to see the value of structuring its operations to make a “systemic impact within a particular location or economic value chain.”⁴⁷

Local Content Strategy—Angola

Ten years ago, the situation in Angola was bleak, with low rates of education, skilled labor, and enterprise development. The country had been torn apart by almost three decades of civil war. The oil industry was the only functioning industry, as the agricultural and financial industries barely functioned. Therefore, the provision of business development services (BDS) was necessary for creating a viable supply chain and improving the ability of SMEs to compete for contracts and provide quality services.⁴⁸ There is no quick fix for the gap in education and skills needed to diversify the Angolan economy, but taking a long-term outlook to build more effective and qualified supply chains is a smart approach that can also provide some positive near-term operational benefits.

In many ways, Angola suffers as it did 10 years ago from the lack of available human capital, local enterprises, and access to credit; with the exception of CAE, there are few providers of high-quality BDS. At the end of 2010, the oil sector was responsible for 58 percent of Angola’s GDP and 80 percent of government revenue.⁴⁹ More work needs to be done to diversify the goods and services side of the Angolan economy, but the economic opportunities rooted in the demand of IOCs are real. Angola still has a long way to go to strengthen its economy outside of oil revenues, but the government’s proactive measures and its partnering with a variety of players has been the driver of the growth of the Angolan economy—and the gains of the oil industry.

Local Content Strategy—The Oil Industry

Because the extraction industry, more than any other, is subject to national mandates to source and hire locally, there was a ready-made market for the goods and services the CAE-trained SMEs were providing. However, even though the mandates in Angola were a catalyst, the process by which local content was developed is what makes this example a success story. Getting host-nation buy-in; formulating a consortium of IOCs to support the provision of BDS and access to finance

44. Wise and Shtylla, “Role of the Extractive Sector.”

45. The \$50 million API was launched in 2002 to support education, food security, government institutional capacity, and small-business development. Through this initiative, and in conjunction with USAID, NovoBanco was formed to provide credit to SMEs. Chevron Human Energy, “Chevron and USAID Pledge New Support for Better Outcomes in Angola: Agreement Latest in Company’s Multimillion Dollar Initiatives in Angola,” August 19, 2009, <http://www.chevron.com/news/press/release/?id=2009-08-10>.

46. Wise and Shtylla, “Role of the Extractive Sector.”

47. This information is in relation to Chevron’s API. For more about this development and investment program, see Business Action for Africa, *Business Partnerships for Development in Africa*.

48. USAID, *Developing the Supply of Financial Services*.

49. Revenue Watch Institute, “Angola: Extractive Industries,” <http://www.revenuewatch.org/countries/africa/angola/extractive-industries>, accessed March 21, 2012.

for local enterprises; and using an entity (public, private, or NGO) to provide technical assistance for SME development are not yet the norm in the industry.

The ideas that were put to work in Angola could translate to the IOCs' business models in other oil-producing countries, but currently the IOCs do not take full advantage of the opportunities available in local sourcing.⁵⁰ The case of Angola also shows that the IOCs can make significant gains from collaborating with each other. Part of the problem in fostering this collaboration could be that the positives associated with it are straightforward (e.g., sharing costs and being able to speak collectively on politically sensitive issues), but the processes necessary to make it happen are less clear.⁵¹ Replicating the best practices from the CAE experiment in other countries has the potential to combat the far-too-prevalent natural curse associated with resource-rich, developmentally poor countries, all the while meeting the private sector's bottom line—cost savings over the long term.

Case Study 2—Tourism: The Spier Group and Local Sourcing in South Africa

Background

Apartheid ended in South Africa in 1993. In the decade that followed, the country underwent a democratization process accompanied by a political push toward black economic empowerment (BEE).⁵² The country's GDP grew at 33 percent from 2000 to 2008. The tourism industry sprang into life as well, growing from 4.6 percent of the country's GDP in 1993 to 8.3 percent in 2006. The industry's boom, however, remained largely confined within white-run and white-operated establishments.⁵³ The Spier Group is an example of a white South African family-run hotel group that got its start at the end of the apartheid. The Group runs, among other things, Spier Leisure, which includes a 155-bed Spier Hotel conference center, two restaurants, and a delicatessen, located in the Western Cape's Stellenbosch Winelands region.⁵⁴

The tourism industry is a cluster of goods and services that incorporates numerous related industries (infrastructure, transportation, construction, hotels, agriculture, restaurants, and crafts), which can create a spillover effect for other sectors. Even though this sector has the potential to stimulate significant local economic development, tourism and hotels in particular tend to use large wholesale retailers rather than smaller enterprises.⁵⁵ There are a variety of reasons for this,

50. Wise and Shtylla, "Role of the Extractive Sector."

51. Ibid.

52. A black-empowered business means more than 25.1 percent black shareholding. Anagaw Dersch Mebratie and Arjun S. Bedi, "Foreign Direct Investment, Black Economic Empowerment and Labour Productivity in South Africa," IZA, Discussion Paper No. 6048, October 2011, p. 8, <http://ftp.iza.org/dp6048.pdf>.

53. SouthAfrica.Com, "South Africa: economy overview," Big Media Publications, accessed December 8, 2011, <http://www.southafrica.info/business/economy/econoverview.htm#ixzz1d8mFCh2R>.

54. Caroline Ashley and Gareth Haysom, "Bringing local entrepreneurs into the supply chain: The experience of Spier," Overseas Development Institute, Project Briefing No. 20, April 2009, <http://www.odi.org.uk/resources/docs/4259.pdf>.

55. Caroline Ashley et al., "The Role of the Tourism Sector in Expanding Economic Opportunity," Economic Opportunity Series, Harvard University, Overseas Development Institute, International Business Leaders Forum, 2007, http://www.hks.harvard.edu/m-rcbg/CSRI/publications/report_23_EO%20Tourism%20Final.pdf.

including a shortage of capacity, poorer quality, and general unreliability. As a result, companies will import goods, services, and skilled labor, which diminish the industry's impact on the local economy. Because the revenue often flows back to foreign investors, the industry has a history of exacerbating income gaps in the destinations it targets.⁵⁶

Drivers

The end of South Africa's political divide catalyzed the country's economic rise. However, even with the BEE legislation, black South Africans were not experiencing the same economic rise that accompanied the country's GDP growth. This was particularly true within the tourism industry.⁵⁷ In 2001, the Fair Trade and Tourism South Africa (FTTSA), a nongovernmental organization, began offering certification of "sustainable tourism"⁵⁸ on a voluntary basis. FTTSA certification focused on labor standards, procurement, and corporate citizenship, with some emphasis placed on environmental impacts and standards.⁵⁹

In an effort to identify the best local sourcing practices within the country's tourism industry, Mboza, a South African tourism company, and the UK-based Overseas Development Institute (ODI) collaborated to start the Pro-poor Tourism Pilot project (PPT Pilots) in 2002.⁶⁰ This program helped facilitate strategies for tourism companies to incorporate a local-content strategy in a way that would benefit their business financially while simultaneously increasing the benefits to the local economy.⁶¹

56. Tanapat Sangaroon and Faikhum Thiraporn, "Poverty reduction through pro-poor supply chains: The role of hotel industry," accessed December 8, 2011, http://iscthlr.turismo.wu-wien.ac.at/files/papers/p100_fullpaper.pdf.

57. In South Africa, black people comprise 74.1 percent of the economical active population (EAP) yet only 18.8 percent are employed. White people make up 12.5 percent of the EAP but they have 68.2 percent of the jobs. Martha Matifadza Nyazema, "Can sustainable tourism development be an important contributor for the success of broad-based black economic empowerment (BBBEE) in South Africa?" European Doctoral Programmes Association in Management and Business Administration (EDAMBA), July 2010, <http://www.edamba.eu/userfiles/file/Nyazema%20%20Martha%20-%20edamba.pdf>.

58. The World Trade Organization defines sustainable tourism as "tourism which leads to management of all resources in such a way that economic, social and aesthetic needs can be fulfilled while maintaining cultural integrity, essential ecological processes, biological diversity, and life support systems." The International Centre for Responsible Tourism, "Cape Town Declaration," August 2002, http://www.capetown.gov.za/en/tourism/Documents/Responsible%20Tourism/Toruism_RT_2002_Cape_Town_Declaration.pdf.

59. Jennifer Seif, "Fair Trade in Tourism South Africa (FTTSA)," Presentation, accessed December 8, 2011, http://www.fairtourismsa.org.za/pdffiles/ITB_Presentation.pdf.

60. There were several PPT Pilots in multiple regions, including sub-Saharan Africa and the Caribbean. Mboza and ODI collaborated on five pilots in South Africa: Spier Leisure, Wilderness Safaris' Rocktail Bay, Sun International's Sun City Resort, Southern Sun's Sandton Complex, and Ker & Downey's safari and hunting sites. The results were compiled into an area guidebook of best practices that were designed to serve as reference guides across the industry. For the South Africa guidebook, see Caroline Ashley, "Facilitating pro-poor tourism with the private sector: Lessons learned from 'Pro-Poor Tourism Pilots in Southern Africa,'" Overseas Development Institute, October 2005, p. 7, <http://www.odi.org.uk/resources/docs/2486.pdf>.

61. The tourism industry's local-content strategies can preserve the cultural identity, thus creating a draw for tourists. If measures are not taken to integrate tourism with other sectors (e.g., music, craft, festival), market opportunity may be lost, and local traditions, which are a source of tourism attraction, will be replaced with an imported lifestyle.

Having supported a number of one-off social projects prior to 2002,⁶² Spier's focus on the principles of social equity and environmental integrity made it a good fit for the project. However, the company also participated in the pilot program to demonstrate the financial benefits that accompanied pro-poor tourism policies and a more widespread adoption of the BEE legislation.⁶³ The leadership at Spier believed that businesses across South Africa were "going to find it increasingly difficult to survive in a market where the customer base is extremely limited by a lack of resources and opportunity."⁶⁴

Activities

With the support from the PPT Pilots, the Group conducted a thorough examination of Spier Leisure's supply chain.⁶⁵ As a result, it systematically changed the procurement process for Spier Leisure holdings in 2004.⁶⁶ While across South Africa, various industries were seeking out opportunities to source from BEE suppliers, Spier's approach went even further. The Group's new enterprise development (ED) procurement approach⁶⁷ set new priorities, established performance indicators, implemented new procurement practices, and measured supply chain performance.⁶⁸ The procurement reform is depicted in figure 1.

The Group also sought out local black entrepreneurs and took steps to support them.⁶⁹ The majority of the contracts the Group issued were for new services in areas such as laundry, petroleum, gas, construction and building, clearing vegetation, collecting firewood, and staffing restaurants.⁷⁰ The first contract sourced through their ED process was with a newly established black-owned business, Klein Begin Laundry. Previously, the Group outsourced its laundry needs, but as the hotel and restaurant grew, so did the costs. The Group decided that it made better financial sense to build the infrastructure onsite and then find a local entrepreneur to run the business; thus Klein Begin Laundry emerged.⁷¹ The Group also found it worthwhile to invest in training of a local black entrepreneur to "clear alien vegetation." Not only did the Group's investment adhere to the goals of the PPT Pilot program, but the costs associated with growing the local business owner's

62. Caroline Ashley, "Facilitating pro-poor tourism with the private sector," p. 3.

63. Ibid., p. 2.

64. Ibid., p. 1.

65. The review was "led by the Sustainability Director with strong support from the owner." Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

66. Gareth Haysom, part-time facilitator, lent support to Spier's procurement reform as a part of the Pro-Poor Tourism Project. DFID's Tourism Challenge Fund funded this position from 2002–2005 in order "to catalyze, demonstrate, and learn from shifts in core business practice in the tourism sector that contribute to poverty reduction." Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

67. Spier's new ED approach combined conventional commercial practices with additional support, such as mentoring, procuring expertise, finance, and clauses to facilitate the employment of formerly unemployed workers. Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

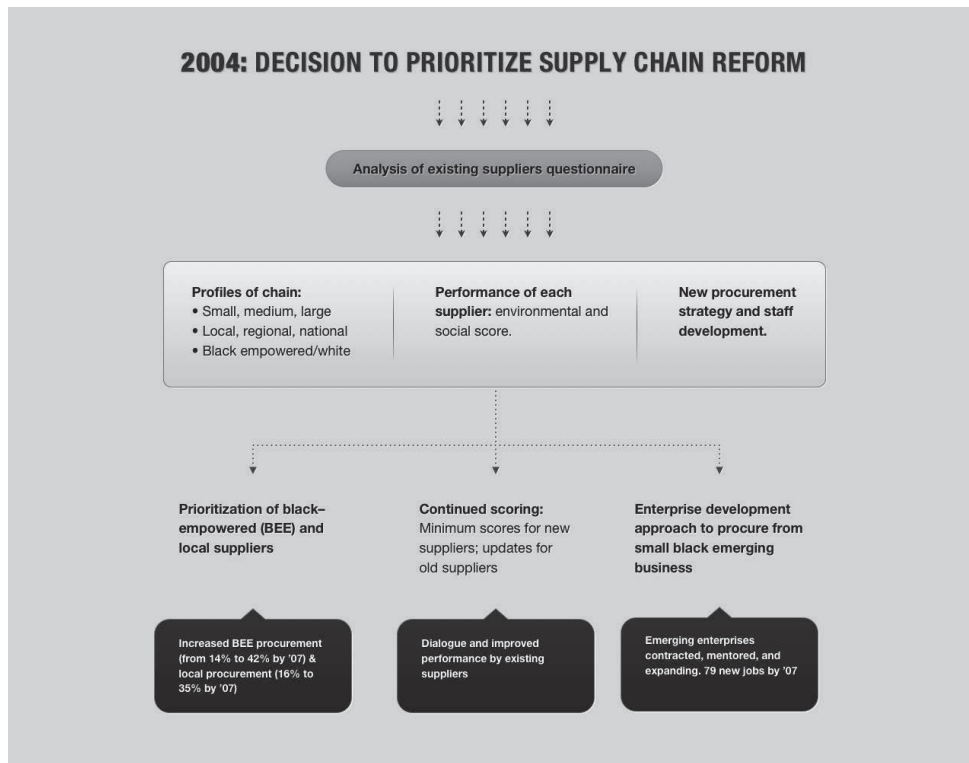
68. Ibid.

69. Spier, "Klein Begin Laundry," September 26, 2011, <http://www.spierblog.co.za/blog/2011/09/26/klein-begin-laundry/>. And Overseas Development Institute, "How to ...? Tips and tools for South African tourism companies on local procurement, products and partnerships. Brief 1: Boosting procurement from local businesses," September 2005, http://www.capetown.gov.za/en/tourism/Documents/Responsible%20Tourism/Tourism_how_to_boost_procurement.pdf.

70. Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

71. Tourism-Review.com, "Tourism: Innovation, Risk-taking, and Protection of Core Business," *Business: Innovations and Risk*, January 2008, <http://www.tourism-review.com/travel-tourism-magazine-business-innovations-and-risks-category375>.

Figure 1: The Process of Strategic Supply-Chain Reform at Spier



Note: Spier’s new ED approach combined conventional commercial practices with additional support, such as mentoring, procuring expertise, finance, and clauses to facilitate the employment of formerly unemployed workers.

Source: Caroline Ashley and Gareth Haysom, “Bringing local entrepreneurs into the supply chain: The experience of Spier,” Overseas Development Institute, Project Briefing No. 20, April 2009, <http://www.odi.org.uk/resources/docs/4259.pdf>.

capacity to meet landscaping needs paid off financially, as the fees were less than what the competitors charged.⁷²

Additionally, the Group took stakes in several companies in its supply chain, including several involving the Group’s employees. Debinisa Transport is an example of a black-empowered joint venture that resulted from the Group’s new approach. This business got its start because a Spier employee approached the Group’s management with a plan to create his own transport company. By working with one of its own transport contractors, the Group helped Debinisa get off the ground by offering the joint venture a portion of its transport business.

This approach also allows less developed SMEs to compete for bigger opportunities. For example, Spier owns the majority stake in a new brick-making business, but intends to sell the company to the employees in the long term. Ensuring sustainability through training and mentoring, the brick-making business has served the Group’s construction needs, as well as created stable job opportunities for local entrepreneurs.⁷³

72. Ibid.

73. Caroline Ashley et al., “The Role of the Tourism Sector in Expanding Economic Opportunity,” p. 34.

Results

The Group's ED strategy combined conventional commercial standards with added benefits that included mentoring and knowledge transfers, assistance with finance and use of the Group's facilities, and contract stipulations requiring the employment of formerly unemployed workers.⁷⁴ In 2004, Spier Leisure received the FTTSA certification, and the ED approach produced measurable development gains. In its first year of implementation, contracts with more than 33 new jobs were created. As of 2006, Spier Leisure was one of only 29 companies to have earned this accreditation, with 41 South African hotels certified through FTTSA in 2011. By 2006, 89 percent of the company's procurement was from businesses with fewer than 50 employees, and more than 90 percent of contracting was with local suppliers. By the following year, the Group more than doubled the amount of local jobs created (79 jobs), with half of the jobs being held by women and 75 percent held by people who were previously unemployed. Furthermore, because most contracts were for new services, Spier did not take jobs from previous suppliers.⁷⁵

Spier not only created new opportunities, but the stability of its contracts also increased the sustainability of jobs in smaller, more vulnerable enterprises. In addition to their ED approach to increase local procurement, the Group increased its direct local hiring and training. Since 2006, the number of permanent employees at Spier increased by 19 percent.⁷⁶ As a part of this increase, it has made efforts to move toward a living wage by 2017. Spier also doubled its investment in training, with more than 90 percent of the beneficiaries labeled as "previously disadvantaged (PD)."

While more labor intensive, the Group's method of locating an opportunity, finding the entrepreneur to fill the gap, and then supplying technical assistance to the local business proved commercially beneficial to the Group as well as to the local economy. This was accomplished at times by taking an initial equity stake in a business with which it worked. This business model optimizes outcomes for both the Group and the local economy. For example, Klein Begin generated four times the local income of the Group's previous arrangement, while the hotel was able to save money through lower prices.⁷⁷ The company continues to work with Spier Leisure in the restaurant and the hotel, handling up to 2,000 to 2,500 items every day during the hotel's high season.⁷⁸ More importantly, the laundry company achieved independent commercial expansion with several new contracts.⁷⁹

In addition, the head of Debinisa Transport went from being a local hire to being a local entrepreneur and contractor—and he was not the only actor to profit from this venture. The Group's original transport contractor was able to qualify as a BEE as a result of this venture, which the Group touts as helping it to "fulfill one of [its] procurement aims."⁸⁰ This business model, accord-

74. Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

75. Ibid.

76. Spier, *Spier Sustainability Report 2010*, Stellenbosch, South Africa, http://www.spier.co.za/spier_sustainability/.

77. Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

78. South African Wine, "Klein Begin Laundry," October 2011, <https://www.kenforresterwines.com/Directory/News.aspx?NEWSID=18879&CLIENTID=1190>.

79. Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

80. Spier, *Spier Sustainability Report 2010*.

ing to a recent ODI report,⁸¹ optimizes the benefits to the local economy as it quadrupled the amount of income in the local economy while allowing the Group to reduce costs by 25 percent.⁸²

Currently, the Spier Group's product offerings include retail outlets, art organizations, hotel services, restaurants, and wine production. Due to the success seen in Spier Leisure's initial supply-chain reorganization, the Group instigated supply-chain reform in other areas, such as its golf and wine holdings.⁸³ Spier provided the seed capital to Primo Vino, a company created to customize Spier's wine bottles in order to comply with international market requirements. Primo Vino now employs approximately 20 people who change the labeling to meet export requirements.⁸⁴ Following this effort, the Group's two wine brands from its Stellenbosch Vineyard, Spier and Savanha, received sustainability awards, and the Spier Group was the first South African winery to receive the South African Wine Industry's Ethical Trade Association Certification.⁸⁵

Spier Wines sources more than two-thirds of its resources from the local community, through hiring practices and local procurement. Using seasonal laborers instead of labor brokers has allowed the wine company to empower the local community instead of importing the hiring opportunities through labor brokers.⁸⁶ Additionally, the two restaurants in the Group's holdings source locally, and their organic food has been rated the highest quality by the South African Sustainable Seafood Initiative.⁸⁷

As a result of these actions, Spier Leisure received international accolades, including the 2011 Sustainable Tourism Award and Condé Nast's Travelers' "Doing It All" award. These highlight the Group's efforts around the environment, individuals, and cultural heritage. In this way the Spier Group is able to leverage these practices to gain competitive advantage because educated visitors frequently seek out companies that benefit local communities

Lessons Learned

The Spier Group

Since its initial push for FTTSA certification and following its participation in the PPT Pilot program, the Group adapted its supply-chain procurement, doubled and tripled the shares procured locally and from "black economically empowered" business, and enabled approximately one dozen local black-owned businesses to enter the supply chain and become established.⁸⁸ Despite its small

81. Spier partnered with the UK's Overseas Development Institute to produce a case study of Spier's overhaul of procurement through supply chain transformation (2004). ODI wrote a project briefing on Spier's work in 2009. Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

82. Spier, *Spier Sustainability Report 2010*.

83. Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

84. Spier, *Spier Sustainability Report 2010*.

85. The Wine Industry's Ethical Trade Association Certification (WIETA) was launched in 2002 to bring together South African stakeholders in the wine industry to find best sustainability practices in the wine trade. Spier, "Our Wines," accessed December 8, 2011, http://www.spier.co.za/our_wines.

86. South African Wine, "Klein Begin Laundry."

87. The South African Sustainable Seafood Initiative was initiated in 2004 in order to educate the country on seafood sustainability issues and to locate best practitioners that support preserving the ocean's ecosystem. Spier, "Hotel Restaurant Wine Bar," accessed December 8, 2011, http://www.spier.co.za/spier_hotel/restaurants/.

88. Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

scale, the Group's efforts in sustainable tourism highlight why local-content strategies are important as well as how to initiate such a restructuring.⁸⁹

By adopting a local-content strategy that fostered a close connection with the providers of local goods and services, the Group demonstrated the value of using a long-term approach rooted in a localized supply-chain reform. The Spier experience features many successful practices that are beneficial for both the local poor and the company's bottom line. Business benefits ranged from cost-saving mechanisms to government and industry recognition, public sector business contracts, and good scoring on the BEE scorecard. The Group, which is an outspoken proponent of its local-content strategy through its blog and in published articles, finds that the "procurement spend is a powerful agent of change."⁹⁰

The company links financial success with strength of leadership, long-term vision, transparency, and good communication. The Group adopted a policy that valued mentorship, improved service standards, payment reform, and smaller contracts, all of which allowed for quick wins. This experience highlighted the importance of the staff using key performance indicators and of training to bring small businesses to scale, which they see as important tips for others.⁹¹ Meanwhile, the stable, sustainable addition of jobs and demand for goods outweighed any possible flow of philanthropic dollars for the development of the community.

Tourism in General

The hotel industry can play a role in economic development as an actor to promote production while generating jobs. The economic development benefits multiply when local content is used in this industry, as new businesses grow, creating the need for more products.⁹² There are frequently low barriers to entry (education, finance, etc.) and women frequently play key roles in the tourism arena. As seen in the Spier Group case, creating a better distribution of income can enhance the lives of the poor while having positive externalities for the tourism industry. By shifting just 10 percent of total procurement, Spier was able to inject more money into the local economy than it had through its traditional philanthropy program. In addition, the shift would create more dynamic impacts that had a multiplier effect beyond that of a much larger philanthropic donation.⁹³

While it may not be plausible to replicate this experience in all environments, the case does indicate the importance of value chain analysis as a key to the sector's economic growth.⁹⁴ Adopting policies that target supply chains work, in that doing so increases commercial returns though cost-saving while simultaneously creating development impacts that far outweigh the benefits of philanthropic flows.⁹⁵ Isabel Hill, deputy director for policy in the Office of Travel and Tourism at the U.S. Department of Commerce, noted the following on Spier's activities:

This is particularly true in the tourism sector, because there is a market advantage to engaging in sustainable practices, as the Condé Nast Award demonstrates. The Spier case repre-

89. Ibid.

90. South African Wine, "Klein Begin Laundry."

91. Sangaroon and Thiraporn, "Poverty reduction through pro-poor supply chains," p. 12.

92. Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

93. Ashley, "Facilitating pro-poor tourism with the private sector."

94. Raphael Kaplinsky and Mike Morris, "A Handbook for Value Chain Research" International Development Research Centre, 2000, p. 9, <http://www.globalvaluechains.org/docs/VchNov01.pdf>.

95. Ashley and Haysom, "Bringing local entrepreneurs into the supply chain"; and Michael Warner, "Reframing 'Local Content' as Local Economic Development," Overseas Development Institute, <http://www.odi.org.uk/resources/docs/848.pdf>.

sents an important development where sustainable practices are integrated into the business model, enhancing the value of the brand in the mind of the consumer, while lowering costs and providing greater control over the supply chain. Thus it provides a more sustainable transactional basis than one based on philanthropy.⁹⁶

As the largest industry in the world, a country's tourism industry provides numerous economic benefits, yet historically, these do not trickle down to the local economy because of the widespread practice of hiring and procuring from imported sources. Examples have shown that these benefits can be more effectively distributed at the local level by strengthening the local supply chain. Local enterprises, farmers, and households earn significantly more when supplying hotel chains with their products.⁹⁷ The multiplier effect of a proper supply chain for the tourism industry is immense. Tourists bring investment, which generates jobs and income for the local people; this improved and sustainable source of income improves health, lowers crime, and decreases corruption within the local community.⁹⁸

Examples are plentiful of hotels and restaurants that cater to tourists in developing nations importing all or nearly all of the food provided to visitors; this is as true for hotels in Jamaica catering to visiting Americans as it is for hotels in Cross River State, Nigeria, catering to Nigerians visiting from other parts of the country. With the goal of increasing the authenticity of the tourist's experience and lowering import costs, hotels and restaurants can use their demand for quality food products delivered in a timely fashion to build supply chains that run from local farmers (who obtain financing based on hotel contracts) to local truckers (whose company's revenues increase with new contracts) to local produce and meat suppliers to the hotels and restaurants. Key to this market-driven support for expanding small-business and farmer income can be the presence of NGOs to provide training to the farmers in quality, management, and other subjects, and to work with them to obtain financing; NGOs may be financed by government agencies or other donors or by the "buyers" (i.e., hotels, restaurants). Rather than use significant levels of donor funding to create a large-scale, agriculture-driven economic growth program that may or may not result in ongoing business for the farmers ("sustainable" or "profitable") let the private-sector players spend their money because they have the promise of a far greater return and the farmers have continuing demand.

Tourism has the ability to diversify an economy in areas where other sectors may be insufficient.⁹⁹ Expanding the tourism industry increases local, state, and federal tax revenues, which can then be funneled back into the community through improved public-utilities infrastructure and transportation infrastructure.¹⁰⁰ From the perspective of the donor, investing in a sustainable business like the Spier Group represents a smart use of funds and the possibility of development and commercial returns.¹⁰¹

96. From author's interview with Isabel Hill, deputy director for policy, Office of Travel and Tourism, U.S. Department of Commerce.

97. Sangaroon and Thiraporn, "Poverty reduction through pro-poor supply chains," p. 5.

98. For example, agriculture. Sangaroon and Thiraporn, "Poverty reduction through pro-poor supply chains," p. 12.

99. United Nations Economic and Social Commission for Asia and the Pacific, "Sustainable Integrated Tourism Planning," accessed December 8, 2011, http://www.unescap.org/ttdw/Publications/TPTS_pubs/Pub_2019/pub_2019_ch1.pdf.

100. Glen Kreag, "The Impacts of Tourism," SeaGrant, p. 6, accessed December 8, 2011, <http://www.seagrant.umn.edu/tourism/pdfs/ImpactsTourism.pdf>.

101. Ashley and Haysom, "Bringing local entrepreneurs into the supply chain."

Case Study 3—Agriculture: SUCCESS Alliance Supporting Smallholder Cocoa in Ecuador

Background

Cocoa prices have risen steadily in recent years and are at or near record highs, representing a great opportunity for smallholder cocoa farmers. Worldwide consumption of cocoa products continues to grow at 2–3 percent or 60,000–90,000 metric tons per year. This includes steady growth in the area of dark and origin chocolates, which command premium prices. Projections show global production remaining behind the increasing demand, indicating that there is a clear opportunity for expanded production of higher-quality cocoa. The cocoa sector, however, faces myriad challenges such as climate change, declining soil fertility, pests and diseases, inefficient farming practices, and political fragility in some of the key supplier countries.

In 2009, Ecuador exported cocoa beans valued at \$335 million, second only to the country's banana exports. Ecuadoran cocoa has a special status on international markets as a high-quality “fine flavor” cocoa garnered by its *Nacional* variety. *Nacional* commands a premium price. In the past, however, cocoa traders and brokers would often mix small-size *Nacional* with CCN51, a lesser-quality cocoa, in order to get a composite higher grade and a premium price. This practice threatened Ecuador's special status on the cocoa market and reduced the potential benefits for thousands of rural cocoa farmers.

In hopes of ensuring the future supply of cocoa, ACDI/VOCA—a global NGO working in the agriculture sector—addressed constraints to sustainable cocoa production and marketing to increase the competitiveness of the sector. Its actions were in recognition of the importance of the cocoa crop to smallholder farmers, as well as the international cocoa industry's need for diversified sources and its increased willingness to invest in capacity-building of the smallholder farmers who supply them.

ACDI/VOCA (A/V) is a founding member of the Sustainable Cocoa Enterprise Solutions for Smallholders (SUCCESS) Alliance, which improves the livelihoods of smallholder farmers by promoting cocoa production and marketing using economically, environmentally, and culturally sustainable methods. The Alliance (which includes local governmental and nongovernmental organizations) receives funding from the U.S. Department of Agriculture (USDA), USAID, and private-sector partners (including the World Cocoa Foundation and its member companies). The SUCCESS Alliance has been active in Ecuador, Liberia, Indonesia, Jamaica, the Philippines, and Vietnam.

SUCCESS Alliance Ecuador

SUCCESS Alliance Ecuador aims to improve farm productivity, increase access to improved planting material, and strengthen farmer organizations. The project began in the provinces of Guayas, Los Ríos, Manabí, and Esmeraldas, and is currently active in Los Ríos and Guayas. The original international donor-funded program was implemented by A/V with international cocoa-buying partners. The cocoa industry, both international and domestic, saw the merits of the initial technical interventions, and as a result, commercial industry contributed to a second program phase in which Ecuador-based donor funding and funding from an international cocoa buyer and processor enabled A/V to continue program interventions for several additional years. An Ecuadoran co-

coa processor and exporter, with cooperation and technical input from international cocoa buyers, funded the program in its latest stage.

USDA (2005–2008) provided the initial support for A/V’s work with SUCCESS Alliance Ecuador with approximately \$5 million. During this phase, A/V helped 21,710 farmers to rehabilitate old, unproductive cocoa trees and replant new, improved cocoa. When the USDA-funded project closed, A/V received additional funding from other sources to continue activities on a more limited scale: the PL480 Corporation (Ecuador government-run using funds from U.S. commodity sales), along with two international cocoa processors and exporters (including the TRANSMAR Commodity Group) and the World Cocoa Foundation (WCF). The third stage, a two-year extension, was funded through a public-private partnership between the National Program for Rural Inclusive Business (PRONERI), sponsored by the Ministry of Agriculture and Livestock (MAGAP) and TRANSMAR. Finally, in 2011, a private export company, Ristokcacao, contributed a 12-month grant to enable the SUCCESS Alliance to continue its work with a focused set of cocoa farmers.

Activities

A/V’s SUCCESS Alliance projects include technical assistance and training through the Farmer Field School (FFS) methodology—which builds social capital in producer communities—with an emphasis on farm planning, crop management, post-harvest management, commercialization, and participation in farmer organizations. Original project objectives were to

- Train 21,000 farmers through FFS to increase the quantity and improve the quality of cocoa;
- Renew and rehabilitate 1 million cocoa trees through the promotion of improved planting material and nursery establishment; and
- Promote the development of 10 farmers’ associations.

The coastal region of Ecuador is populated by farmers known for their individualism and the region does not have a strong tradition of farmer associations or collective marketing. Although some associations did exist, they were the exception rather than the rule and required heavy project input and follow-up. A/V brought together small cocoa farmers for the first time for many, building social capital as farmers got to know their neighbors through six months of FFS training. The FFS provided farmers with the opportunity to carry out group work on practical exercises designed to teach improved crop husbandry. This enabled farmers to trust each other as farmers and neighbors and inspired many to organize themselves more formally.

A/V had a local team on the ground to manage this process. Initially a resident team of 15 managed the project, but by the final phase of the program, the team was reduced to four full-time staff members complemented by technical consultants on short-term assignments.

Results

Seedling Production. Farmers trained in FFS produced more than 6 million seedlings at nurseries owned and operated by farmers and farmer associations. They also rehabilitated 1,519 hectares of old, unproductive cocoa trees and replanted 1,293 hectares of cocoa. *The estimated value of the investments by farmers trained in FFS exceeds \$4 million.*

Considering the number of nursery-grown cocoa plantlets (roughly 6 million), at a planting density of 1,111 plants per hectare, the estimated cocoa area renovated by plants resulting from project training surpasses 5,500 hectares. This significant area of productive cocoa farms ensures a greater volume of high-quality cocoa to Ecuador's exporters and the world's consumers. Farmers realizing the benefits of collective action are leveraging group purchasing and selling to improve their access to lower-priced fertilizers and tools, to improve the quality and quantity of their production, and to get a better price in the marketplace for their product.

Cocoa Plantlet Production. The project did not originally have a goal in propagating nursery plants; the proposed objective was to provide technical assistance to 27 association nurseries established during the first project phase to ensure that they continued working on a commercial basis. However, the project also provided technical assistance via extension agents to many others requesting such support.

Farmers propagated 1.6 million cocoa plantlets in 122 nurseries with seasonal sales approaching \$800,000. It is noteworthy that 93 percent of the plants propagated are fine-flavor cocoa *Nacional* variety and only 7 percent are CCN51. The farmers have a new-found opportunity to be paid a premium for a superior product, and they are investing in quality and the variety preferred by international buyers.

Farmer Training. FFS trained 21,710 farmers in cocoa-crop husbandry and post-harvest handling through 872 FFS.¹⁰² During the first phase of the project, 6,600 farmers participated in field days and cocoa fairs that complemented the training and increased farmers' sense of how the larger industry worked to produce, process, and commercialize their cocoa. Field days and cocoa fairs allow industry equipment and service suppliers, grower cooperatives, and industry experts to network and build professional relationships. Their business deals during and after the fairs help the industry strengthen business relationships and improve its overall performance.

Integrated Crop Management and Bio-control Research. The SUCCESS Alliance signed and financed an agreement with the National Agriculture Research Institute (INIAP) Pichilingue Experimental Station to conduct integrated crop management (ICM) and bio-control field trials on smallholder cocoa farms. These trials proved that ICM and the application of bio-control agents (*Trichoderma* species) can control witch's broom and frosty pod rot. These two diseases cost cocoa farmers in Ecuador an estimated \$50 million in losses per year and are a main reason for cocoa yields being among the lowest worldwide. The bio-control agents available for testing were first researched at the USDA's Beltsville, Maryland, station with support from Mars, Inc. and the INIAP Pichilingue facility. The trials tested these agents under smallholder farmer conditions.¹⁰³ Cocoa is a perennial crop that takes 1.5–2 years to start producing and four to six years to reach stable production after ICM changes have been made. This work must be conducted over a period of five to seven years to generate reliable data; direct funding from chocolate-manufacturing firms has continued the work.

102. The FFS methodology is an interactive, hands-on approach to learning in which farmers choose priority topics to be covered with the guidance of a trained facilitator.

103. Additionally, the objective of INIAP's field trials was to determine what effect ICM practices and disease management have on cocoa pod production when combined with the use of bio-control agents and fertilization.

Farmers' Association Strengthening. In spite of the challenging process of forming a legal farmers' association, the project strengthened 75 cocoa farmers' associations and formed 30 new associations. These associations enabled farmers to achieve economies of scale by buying inputs and selling cocoa collectively. SUCCESS Alliance Ecuador monitored associations' progress and provided training and technical assistance to encourage the associations to use a business approach to ensure sustainability. Members were taught their rights and responsibilities to the association. Rights included having fair and consistent access to information about the activities of the association and responsibilities included participating actively in meetings and group activities. The business-training plan was structured around three subject areas delivered in seven workshops to each participating organization:

- Principles of cooperative and association;
- Farming as a business; and
- Developing business and marketing plans.

Collective Marketing. In 2006, the SUCCESS Alliance project began to provide marketing assistance to smallholder cocoa farmers, resulting in a more formal associative marketing program supported by an international chocolate manufacturer. At this point, few farmers' associations marketed their cocoa collectively; the majority of cocoa farmers followed the traditional practice of selling individually to local traders at steeply discounted prices. With project support, two cocoa farmer associations, Rancho Grande in Los Ríos, and APROCA in Esmeraldas, filled and sold a 25-metric-ton container of cocoa over a period of four months following strict quality guidelines and a rigorous sampling process.

The following year, SUCCESS Alliance's association marketing worked in two areas:

- The project worked with eight communities comprising 68 farmers in Naranjito, Guayas. During a six-month period, these communities sold \$115,000 of good-quality, fermented, dry cocoa directly to Guayaquil exporters. By working and selling cocoa together, they made \$25,000 more than they would have by selling to local brokers.
- Rancho Grande-Vinces, in Los Ríos Province, an association formed by 26 farmer members, sold 36.8 metric tons of cocoa to exporters at an average 23 percent premium over the price paid by local traders, resulting in additional income of \$11,618.

Observed Cocoa Marketing Problems

Collective marketing support was not originally envisioned under the project. However, as the project expanded, the following problems in the marketing system became evident:

- *Unfair prices*—Many farmers received a very small percentage of the export price.
- *Low grading*—Individual smallholder farmers' cocoa was unfairly discounted by some local cocoa traders.
- *Unfair weighing*—"Fixed" weighing scales in many areas benefited unscrupulous cocoa buyers at the expense of smallholders.
- *No incentive for high quality*—Most local buyers bought unfermented, contaminated, low-quality cocoa and mixed varieties for volume; field buyers had historically not paid farmers more for higher-quality cocoa.

- The phenomenon of farmers marketing through associations continued to grow in subsequent years as farmers discovered the return on investment from working together on quality production, handling, and collective marketing.

Lessons Learned

The Need to Expand Supply. While the world market demand is rising, particularly in the premium market segment of origin chocolate products, global supply is limited and threatened by climate change and political fragility in some of the key supplier countries. The international cocoa-buying firms are increasingly willing to invest in capacity-building of the smallholder farmers who supply them, in hopes of ensuring future supply. The international nongovernment organization (INGO) is well placed internationally to channel commercial investment into rural capacity-building.

Donor-funded Initiative, Private-Sector Follow-through. The firms wanted ongoing improved performance from their supply-chain partners. Public funding of INGO proved the worthiness of investing in training and group organizing, so those businesses stepped in and financed the INGO to continue such industry development and capacity-building. The businesses partnered with the INGO to deliver additional technical trainings in cultivation, post-harvest handling, and quality control.

Institutional Strengthening Work Is Slow. Strengthening farmer associations is a slow process that can take several years and requires careful technical assistance. It involves changing smallholder farmers' ways of thinking and working to get them to see that the best way for them to increase production, raise farm yields, and improve their living conditions is by working together in a well-organized manner. A three-year horizon is often insufficient to achieve sustainable institutional change.

Strength through Associations. Cocoa is a perennial tree crop that takes time to respond and start producing in response to new crop-husbandry practices. Smallholder farmers cannot prune their entire farm all at once as they need production from some of their trees for living expenses. This simple fact encourages farmers to prune their cocoa plantings gradually, over several years. Through farmer associations, farmers are able to spread labor and other costs over several years and keep a portion of their cocoa plantings in production, thus providing necessary ongoing income.

Value of Alliance Communication. The SUCCESS Alliance enabled ACDI/VOCA to communicate to international buyers the story of Ecuador's struggling smallholder cocoa farmers. The resultant attention and contribution—both monetary and technical—from the industry's big buyers allowed ACDI/VOCA to continue to work for improved outcomes for Ecuador's smallholder farmers. The international buyers also benefited from higher numbers of reputable exporters and higher aggregate tonnages of premium cocoa supply. In a tight international cocoa market, Ecuador's export figures are growing.

Reduced Funding Shrank Project Reach. In 2008, the project sourced new funding from the PL480 Corporation and TRANSMAR,¹⁰⁴ but at lower funding levels. The project leveraged its experience acquired during the first three years of work, cut costs by reducing personnel and project

104. SUCCESS Alliance Ecuador was supported by USDA funding for direct project activities until December 2008.

The Coca-Cola Company and East African Fruit Farmers—Investing in Regional Capacity to Meet Fruit Juice Demand

The domestic demand in East Africa for processed fruit is growing. To capitalize on this trend, The Coca-Cola Company imported fruit concentrate needed for its local factories to produce drinks sold in East Africa. Even though locally produced fruit-juice concentrate costs up to 50 percent less than imported concentrate, there was an insufficient local supply to meet Coca-Cola's needs (and those of other multinational corporations).

To enable productivity and reduce import costs, Coca-Cola signed onto a four-year project on January 20, 2010, to develop the capacity of 50,000 mango and passion fruit farmers in Uganda and Kenya. With \$7.5 million from the Bill & Melinda Gates Foundation and \$4 million from Coca-Cola's Central, East, and West Africa (CEWA) Business Unit, this initiative is the first of its kind on the agricultural side of Coca-Cola's vast supply-chain network. The beverage giant enlisted TechnoServe, a U.S.-based NGO specializing in providing technical assistance, to work with the small fruit farmers to increase their productivity. Through training, quality improvements, and facilitating access to credit, this project is designed to bridge the gap between East Africa's fruit farmers and the market opportunity provided by Coca-Cola. The goal is to positively impact the development of several communities and provide Coca-Cola with locally harvested fruit for its popular regional fruit-juice products.

As of November 2011, the project has successfully mobilized more than 37,000 mango and passion fruit smallholder farmers in both Kenya and Uganda, increasing the average metric tons of mangos and passion fruit sold in Kenya and mangos sold in Uganda. This innovative agriculture partnership is expected to double the fruit farmers' incomes by 2014. However, sourcing and processing the fruit locally is also a smart business move for Coca-Cola. Processed fruit consumption is growing at 6 percent annually in Africa.

As a result of Coca-Cola's access to locally produced fruit, a Minute Maid nectar and juice drink, which uses the Ngowe-variety mango from Kenya, is now available in multiple markets across Africa. Nathan Kalumbu, president of Coca Cola's CEWA business unit, explains, "This partnership is a great example of sustainability. By partnering with tens of thousands of local farmers, we can help increase their incomes while meeting our needs for locally sourced fruit, benefiting both the community and our business." This project and the lessons learned from it serve as a partnership model for Coca-Cola as it grows its juice business in other markets.

reach, and worked only in more accessible areas. The overall goal of the scaled-back project was to work with the 2,500 most-motivated farmers, those who were willing to work with their fellow farmers to rehabilitate their farms, market their cocoa collectively higher up the value chain, and learn the concepts of "farming as a business" in order to diversify their farms and income streams.

- In 2008 the project helped 122 cocoa nurseries produce 1,568,000 seedlings, 92 percent of which are *Nacional* variety. Additionally, through the associations, participating farmers pruned 2,956 hectares of cocoa in 2008, equivalent to an investment of more than \$1,182,000 in their farms.

- The project trained 1,893 farmers in association strengthening in 2008. The project provided training in association and cooperative principles and in marketing and business-plan development to members of 70 associations, 65 of which obtained legal status as a result of project support.
- One thousand smallholder farmers from five communities participated in associative marketing and sold 335 metric tons of cocoa. They received \$135,000 more in proceeds by selling collectively and directly to exporters than they would have received by selling individually.

3

RECOMMENDATIONS

In addition to the lessons learned and recommendations associated with the case studies in chapter 2, the two working group sessions, research, and interviews revealed a range of insights and recommendations. Among the recommendations are those applicable to the private sector, to the U.S. government entities operating in developing states, and to host-country governments.

1. U.S. government and other donor agencies

In addition to the specific recommendations for U.S. government agencies presented earlier in this paper, there are unique opportunities for donor agencies to help shape and maximize the development impact of multinational corporations, or MNCs, and other corporate players. Certainly some of the agencies are well placed to bring together diverse players—private-sector MNCs and local businesses of all sizes, U.S., foreign, and host-government agencies, and international and local NGOs. This is an invaluable role and one that can use the expertise of donor agencies along with incremental funding inputs to maximum effect.

- **Collaborate.** Private-sector initiatives maximize the economic development impacts of their plans and operations, and perform by going beyond their core business functions and assets and reaching out to the public sector, NGOs, donor agencies, and philanthropies for knowledge, experience, and funding. Partnering with large competitors (as in Angola’s CAE or the World Cocoa Alliance) is frequently desirable but is often difficult to actualize. “Collaboration allows parties to share knowledge and information, pool scarce or diverse assets and resources, access new sources of innovation, create economies of scale, and enhance the legitimacy of the parties’ own individual activities. In addition to assembling the necessary resources and capabilities, collaboration can generate new capabilities and change operating environments in ways that create new strategic opportunities.”¹⁰⁵
- **Recognize the different motivating forces.** Recognize the different motives and drivers of large buyers of goods and services, the local suppliers of those goods and services, donors (governments and foundations) that can support local SMEs with technical assistance and financing, and the host government. Transparency of motives is important and the motivations themselves can be different, but the outcome—development impact—can be the same or similar. By recognizing this, the various interests can weave an approach that maximizes positive impact on SMEs and the large buyers. The important role of “driver identification” is an excellent one for development agencies.
- **Be flexible in interventions and tools.** In Angola the international oil companies were willing to work together and finance much-needed training; just a few years earlier in Azerbaijan, USAID had to fund a similar training program that ultimately gained buy-in from the oil

105. Wise and Shtylla, “Role of the Extractive Sector,” p. 5.

companies. In one sector or with one MNC's business unit, financing training may be acceptable, but funding the construction of a storage facility is outside the corporate bounds; while in another setting, financing the construction of the last mile of good road to get goods to market is within the corporate vision, but training suppliers is not. Filling the gap with timely financing can produce benefits with exceptional multipliers.

- **Plan activities in commercially viability terms.** “Free-standing” technical assistance, manpower training without existing or realistically anticipated demand, and like can be worse than doing nothing—producing significant frustration, disappointment, wasted opportunities, and un-recoupable expense. Value comes from linking technical assistance (as well as training for business management, access to finance, business linkages, etc.) for local businesses to potential end-users of the newly trained companies. When possible, reach out to the end-users to contribute to the cost of the training or to provide their own experts to provide part of the training. While more complicated, the payoff is there in opportunities for the local firms and in firm-level and supply-chain growth and success, effective cost management, and long-term sustainability for the end-users.
- **Build lists of local sources.** Information may be the most valuable commodity in overcoming barriers to entry into global supply chains. Recognizing possible competitive issues, a communal list of viable local sources within a sector could improve efficiency and help lower one of the barriers to participation in local sourcing. A more comprehensive list of trained and qualified suppliers could be made available across industry sectors, erasing the impact of sector stove-piping that prevails today.

2. Private sector

- **Provide business training and build local capacity.** One should build capacity at the time capital is provided. Invest time in fostering entrepreneurship and executive-development activities. There is a lasting impact of skills development and training on a local economy. Companies that provide and support business, management, or manpower training will foster a more skilled business community that will not only support its efforts as contractors but will also, in turn, create a business environment that will be more enticing to new business operations and new investment.
- **Contracting vs. hiring.** While individual employment provides a positive impact for individual families and local economies, the use of contractors is far more development-effective. While the individual will learn on the job, his or her time is spent in executing an assigned role; a small business with a new contract will look for other buyers of its products or services, whether with other buyers in the same industry or in a different sector—and, over time, with buyers in different countries.
- **Achieve results without sacrificing quality.** When procurement officers in the private and public sector discuss relying on local content, they focus on the concern of sacrificing quality. There are acceptable expenditures for local training, there is recognition of the need for far more information for the local business community and better and more timely communications, and there may be opportunities to build slightly slower deliveries into the supply-chain schedule or break large purchasing packages into smaller packages from multiple local sources. But anyone working to grow the local content of goods and services for major end-users must understand that quality is king. The ability to aggregate the production of large numbers of

smallholder farmers in a sustainable fashion is often key to overcoming the reluctance of MNCs to purchase locally. (This is not limited to traditional business—in Afghanistan, local purchasing by military contracting officers is now a part of counterinsurgency.)

- **Analyze commercial benefits, corporate drivers.** One of the working group participants called for an in-depth study of the commercial benefits accruing to MNCs and others using bottom-line decisionmaking to support local economic development. Documenting the various short- and long-term benefits of many local-content development programs will make the argument for replication. Linked to this was the suggestion by another participant to analyze the corporate drivers in each business sector and link them to program outcomes.
- **Size matters.** Today there are relatively few companies designing and implementing the bottom line-driven/development impact programs and they are generally among the largest corporate players. Often they are also the companies seen as leaders in their industry sectors in specific and commerce in general—their strategies and their activities are followed by colleagues and by competitors around the world, and their best practices are both recognized and emulated. One measure of change will be based on the number of large, well-known MNCs incorporating these strategies; another will be when more and more medium-size players operating in the global environment incorporate them.
- **Do not forget the “micros.”** There are many small businesses that may not meet the standards and qualifications necessary to participate in large company procurements, but can supply and support local firms that are qualified and participate in contract procurements. Whether they supply manpower or basic services, or purchase products and services from the newly qualified, they play a role; allowing them to participate in training programs can produce long-term benefits to the local economy and commercial environment.
- **Move beyond tactical.** Work with local consulting firms, local economic developing and investment-attraction agencies, and local institutions that are going to be able to generate those capacities that will go beyond the two- to three-year short-term “tactical” needs.
- **What goes into the bottom line.** This paper focuses on corporate decisionmaking with development outcomes driven by traditional bottom-line elements—faster, cheaper delivery of goods and services, reduced risks for doing business, meeting host-government mandates, building brand identification, etc. One of the working group participants argued that there is a significant need to *quantify* social factors along with the traditional financial components of bottom-line decisionmaking if large, international firms were going to consistently involve development in their calculations—for example, “valuing green buildings” in an MNC assessment regime.

3. Host governments at all levels

- **The U.S. government and private sector should work with host governments.** The purpose would be to ensure that their policies and regulations maximize local firms’ ability to participate in global supply chains. MNCs need an in-country enabling environment that supports local contracting and working with NGOs and business services groups; SMEs need supportive registration, taxation, ownership, education, and banking policies (from the Central Bank down to small-business lending practices of local banks that enhance access to finance).

- **Each level of a host government presents different challenges.** Local governments may be too focused on tactical, short-term goals; and national governments may be too removed and political. The regional governments may provide an underutilized avenue for effective partnerships.
- **More mandates?** Going forward, planning and strategies need to take into account possible increases in host-government mandates, especially into new sectors (e.g., information technology). In oil and gas, the rise of the power of state oil companies will also affect the landscape. As one of our working group participants recognized, there would be great value in looking at the true impact of mandates, sector-by-sector, environment-by-environment—whether mandates actually distort or even inhibit developmental impact. Another working group participant argued that some companies would build out different or better supply chains, were it not for mandates. Obviously mandates have had a positive impact in at least some extraction-driven development and it is timely to look at what might have been accomplished with or without mandates.

4

CONCLUSION

Across a wide spectrum of industries, implementing a local content strategy—which can involve a large number of measures to maximize local contracting for goods and services in new or existing national and global supply chains—is one of the most effective and sustainable development strategies that companies can use and U.S. government agencies can support. Often, local enterprises in the developing world have an extremely limited ability to provide goods and services consistently, on time, and to the standards demanded by international firms. A lack of experience with transparent procurement policies and limited access to timely information, competitive business skills, and finance are among the barriers to entry that greatly inhibit local participation. Much of this, however, could be overcome with a local-content strategy.

A well-formulated—and properly executed—strategy should contribute to the economic base that would then create a new generation of quality businesses able to service multiple sectors and meet the needs of domestic customers and consumers for future activities across the developing world.

There is a compelling business case—with short- and long-term returns—for implementing a comprehensive local-content strategy. Doing so helps to build market-based economies, generate economic opportunities, and stabilize communities in countries where businesses operate and where the United States has strategic interests. In addition, procurement and operating requirements raise performance and quality standards of all SMEs involved in training and competing for contracts—over time, the local firms (and their competitors) apply these higher standards to their performance when they serve local commercial buyers and local consumers whose expectations then begin to rise.

At the same time, a number of U.S. government agencies already have programs and resources to develop local content, ranging from initiatives that build the capacity of entrepreneurs and enterprises to programs that increase access to markets and to financing. These types of activities should be expanded, coordinated with other institutions, and linked with the activities of “end-users” of the goods and services. They should be prioritized in every field mission with greater access to best practices. The stability and economic growth of developing world countries is not only important to the United States from a development-policy standpoint, it is also increasingly intertwined with U.S. economic growth and U.S. national security.

We are in the very early stages of corporate strategies and practices intentionally linking bottom-line decisions and local-content policies with economic development in countries with developing or frontier economies. The numbers of proactive MNCs or major local companies remain relatively small, but their successes, their identification as innovative industry leaders, and the needs of many, many more global businesses hold great promise. At the same time, the changes at some development agencies and donor organizations that are leading to public-private partnerships and support for market-driven solutions also hold promise for new, integrated approaches

that will allow those agencies and organizations to use targeted, timely, country- and project-specific interventions in order to accomplish far more for the peoples, families, and businesses of developing nations using far fewer public resources. As government agencies and donors see the enhancement and facilitation of the development of local content and capacity in a more targeted way, tied directly to the activities of the private sector, development outcomes will be significantly enhanced.



ABOUT THE AUTHORS

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Michael Levett is currently senior director and vice chair of the board of directors of CDC Development Solutions. He joined what was then Citizens Democracy Corps in 1994 as its president and in the intervening years led the company's expansion into more than 80 countries on five continents. Prior to joining CDS, he developed and managed trade, cultural, and commercial ventures in the countries of the former Soviet Union and Central Europe. He then returned to Washington, D.C., to serve as the founding president of Business for Social Responsibility, today's leading business organization that develops and disseminates socially responsible corporate strategies to businesses of all sizes and industries and that links socially responsible practices and competitive companies. Mr. Levett was also vice president at two international film companies, Lucasfilm, Ltd., and Dino DeLaurentis Corp. He was a reporter for the *Los Angeles Times*, a White House Fellow, and a Loeb Fellow at Harvard University with a focus on environmental and regional planning issues. He holds BA and JD degrees from UCLA. Mr. Levett is chairman of the Board of Directors of the Volunteers for Economic Growth Alliance (VEGA), a member of the Executive Committee of the Small Enterprise Assistance Funds, a member of the Bretton Woods Committee, and a non-resident fellow at Georgetown University's Institute for the Study of Diplomacy.



ABOUT THE PROJECT

The Project on U.S. Leadership in Development is a partnership with Chevron Corporation focused on leveraging all U.S. assets—the private sector in particular—to promote economic development, improve livelihoods, and reduce poverty worldwide. The project seeks to renew the discourse in Washington and develop a fresh, actionable set of policy recommendations for 2012 and beyond. The project builds on the ongoing work of CSIS in global health, water, trade, food security, governance, and economic development in the areas of conflict and post conflict.

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